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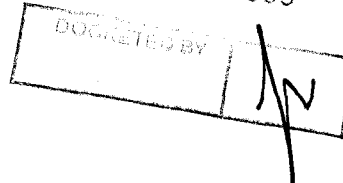
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ARIZONA CORPORATION COMMISSION

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January 13, 2000
AZ CORPORATION COMMISSION
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Arizona Corporation Commission
DOCKETED

JAN 26 1999



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The Honorable Janet A. Napolitano
Attorney General
1275 West Washington
Phoenix, Arizona 85007

Re: A.A.C. R14-6-101 through R14-6-104, R14-6-106, R14-6-201 through R14-6-203,
R146-205 through R14-6-212

Dear Ms. Napolitano:

The above-referenced rules were repealed and replaced on January 10, 2000, by the Arizona Corporation Commission ("ACC"), subject to approval by the Attorney General. Assistant Attorney General Robert Zumoff was consulted during the drafting of the new sections. Mr. Zumoff reviewed the rules and provided his informal comments.

The following information is provided for your use in reviewing the enclosed rules for approval pursuant to A.R.S. § 41-1044:

I. Agency Rules Not Published in Code

To my knowledge, the only Securities Division rules not yet published in the Code, other than this rule, are the Securities Division's new sections R14-4-139, R14-4-143, and R14-6-204, and amended rules R14-4-101, R14-4-102, R14-4-127, R14-4-133, R14-4-134, R14-4-141, R14-4-144, which are currently awaiting approval by your office, and new section R14-4-126, which was forwarded by your office to the secretary of state on September 28, 1999.

II. Procedures Followed

The ACC's rulemaking process was as follows:

- (1) A Notice of Rulemaking Docket Opening was published in the Arizona Administrative Register in 4 A.A.R. 1290, June 5, 1998, regarding A.A.C. R14-6-101 through R14-6-104 and R14-6-201 through R14-6-210.
- (2) A Notice of Rulemaking Docket Opening was published in the Arizona Administrative Register in 5 A.A.R. 623, February 26, 1999, regarding R14-6-101 through R14-6-104, R14-6-106, and R14-6-201 through R14-6-212.

1200 WEST WASHINGTON, PHOENIX, ARIZONA 85007 / 400 WEST CONGRESS STREET, TUCSON, ARIZONA 85701

www.cc.state.az.us

- (2) A Notice of Proposed Rulemaking was published in the Arizona Administrative Register in 5 A.A.R. 1204, April 30, 1999.
- (3) The Notice of Proposed Rulemaking provided notice of the public hearing (oral proceedings) for the rule. In addition, on May 26, 1999, and June 2, 1999, the ACC posted notice of the public hearing in compliance with Arizona open meeting laws.
- (4) The Notice of Termination of Rulemaking in connection with the repeal and remaking of A.A.C. R14-6-204 was published in the Arizona Administrative Register in 5 A.A.R. 2378, July 23, 1999.
- (5) Public participation pursuant to A.R.S. § 41-1023 was as follows:
 - (a) The ACC accepted written comments through June 10, 1999, the date of the public hearing.
 - (b) There were no requests for oral proceedings; however, the ACC scheduled oral proceedings for the rule.
 - (c) A public hearing (oral proceedings) occurred on June 10, 1999.
- (6) The ACC closed the record on the rule at its January 5, 2000, open meeting.
- (7) The ACC adopted the rule by unanimous vote during the January 5, 2000, open meeting. The signed order adopting the rule is dated January 10, 2000.
- (8) The ACC complied with the open meeting laws, where applicable.
- (9) There are no other procedures specifically required by the ACC's statutes.

III. Supporting Documents

I have enclosed, for your information, the following documents:

- (1) Original and four copies of the Notice of Final Rulemaking, including the preamble and text of the new rule.
- (2) Original and four copies of the Concise Explanatory Statement.
- (3) Original and four copies of the ACC's Agency Certificate.
- (4) One copy of 17 CFR 275.204.2 (1998) incorporated into A.A.C. R14-6-101(B)(16) by reference.

- (5) Original and three copies of the ACC's Agency Receipt.
- (6) Original form for Attorney General approval of final rules.
- (7) One copy of each of the Notices of Rulemaking Docket Opening, as published.
- (8) One copy of the Notice of Proposed Rulemaking, as published.
- (9) One copy of the procedural order for the June 10, 1999, public hearing.
- (10) One copy of the transcript of the public hearing on the rule.
- (11) One copy of the ACC order approving the rule subject to Attorney General approval.

Under A.R.S. § 41-1055(D)(3), the ACC is not required to prepare an Economic, Small Business And Consumer Impact Statement for this rulemaking. The Division has, however, prepared and enclosed an original and four copies of an Economic, Small Business And Consumer Impact Statement because we anticipate that your office will require such a statement as it did in connection with the A.A.C. R14-6-204 rulemaking, a rulemaking similar to this one.

Please let me know if you would like any additional copies of these items. We have included a disk containing the Notice of Final Rulemaking in rich text format for the secretary of state. My understanding is that you will forward the final rulemaking packet (including the disk) to the secretary of state.

Please let me know if I can be of any assistance to you in your review process. My direct line is 542-0643. You should also feel free to contact Cheryl Farson, General Counsel for the Division, at 542-0193. Thank you for your cooperation.

Very truly yours,



Mark Sendrow
Director of Securities

cc: Chairman Carl J. Kunasek (w/o encl.)
Commissioner Jim Irvin (w/o encl.)
Commissioner William A. Mundell (w/o encl.)
Brian C. McNeil, Executive Secretary (w/o encl.)

NOTICE OF FINAL RULEMAKING

TITLE 14. PUBLIC SERVICE CORPORATIONS; CORPORATIONS AND ASSOCIATIONS;

SECURITIES REGULATION

CHAPTER 6. CORPORATION COMMISSION--INVESTMENT MANAGEMENT

PREAMBLE

- | <u>1. Sections Affected</u> | <u>Rulemaking Action</u> |
|-----------------------------|--------------------------|
| A.A.C. R14-6-101 | Repeal |
| A.A.C. R14-6-101 | New section |
| A.A.C. R14-6-102 | Repeal |
| A.A.C. R14-6-102 | New section |
| A.A.C. R14-6-103 | Repeal |
| A.A.C. R14-6-103 | New section |
| A.A.C. R14-6-104 | Repeal |
| A.A.C. R14-6-104 | New section |
| A.A.C. R14-6-106 | New section |
| A.A.C. R14-6-201 | Repeal |
| A.A.C. R14-6-201 | New section |
| A.A.C. R14-6-202 | Repeal |
| A.A.C. R14-6-202 | New section |
| A.A.C. R14-6-203 | Repeal |
| A.A.C. R14-6-203 | New section |
| A.A.C. R14-6-205 | Repeal |
| A.A.C. R14-6-205 | New section |
| A.A.C. R14-6-206 | Repeal |
| A.A.C. R14-6-206 | New section |
| A.A.C. R14-6-207 | Repeal |
| A.A.C. R14-6-207 | New section |
| A.A.C. R14-6-208 | Repeal |
| A.A.C. R14-6-208 | New section |
| A.A.C. R14-6-209 | Repeal |
| A.A.C. R14-6-209 | New section |
| A.A.C. R14-6-210 | New section |
| A.A.C. R14-6-211 | New section |
| A.A.C. R14-6-212 | New section |
2. The specific authority for the rulemaking, including both the authorizing statute (general) and the statutes the rules are implementing (specific):

Authorizing statute: A.R.S. § 44-3131

Implementing statute: A.R.S. §§ 44-1801, 44-3101, 44-3132, 44-3133, 44-3153, 44-3156, 44-3201, 44-3212, 44-3213, 44-3241, 44-3292, and 44-3296

Constitutional authority: Arizona Constitution Article XV §§ 4, 6, and 13

3. The effective dates of the rules (if different from the date the rules are filed with the Office):

The rules are effective as of the date filed with the office of the secretary of state.

4. A list of all previous notices appearing in the Register addressing the final rules:

Notice of Rule Making Docket Opening 4 A.A.R. 1290, June 5, 1998

Notice of Rule Making Docket Opening 5 A.A.R. 623, February 26, 1999

Notice of Proposed Rulemaking 5 A.A.R. 1204, April 30, 1999

Notice of Termination of Rulemaking regarding
A.A.C. R14-6-204 5 A.A.R. 2378, July 23, 1999

5. The name and address of agency personnel with whom persons may communicate regarding the rulemaking:

Name: Cheryl T. Farson, General Counsel

Address: Arizona Corporation Commission, Securities Division
1300 W. Washington, Third Floor
Phoenix, AZ 85007-2996

Phone: (602) 542-4242

Fax Number: (602) 594-7470

6. An explanation of the rules, including the agency's reasons for initiating the rules:

The Arizona Corporation Commission (the "Commission") repeals and replaces Sections R14-6-101 through R14-6-104 and R14-6-201 through R14-6-209 and adds new Sections R14-6-106 and R14-6-210 through R14-6-212 (collectively the "IM Rules") in order to: (i) correct

technical errors within the Sections; (ii) reflect amendments to the United States Securities and Exchange Commission rules regarding the regulation of investment advisers and investment adviser representatives; (iii) provide for the distribution of information regarding products and services on the Internet; (iv) clarify the statutory definition of investment adviser representative; (v) prescribe parameters to the term "solicit" as used in the Arizona Investment Management Act adopted in April 1994 (the "IM Act"); and (vi) clarify filing requirements for licensure and notice filings. A brief description of the Sections covered by this rulemaking follows:

R14-6-101. Definitions: defines various terms used through the Sections.

R14-6-102. Scope of Provisions: states the legal authority for the Sections, provides for the waiver of strict adherence to a provision, and provides that the Arizona Corporation Commission's rules of Practice and Procedure apply when not in conflict with the proposed Sections.

R14-6-103. Severability: establishes the severability of the Sections and the provisions thereof in case any Section or subsection is deemed to be invalid.

R14-6-104. Enforcement of the Arizona Investment Management Act: provides that the Sections relating to enforcement matters are Sections A.A.C. R14-4-301 through R14-4-308.

R14-6-106. General Dissemination of Information on the Internet: establishes the circumstances under which investment advisers and investment adviser representatives may distribute information regarding products and services on the Internet prior to licensure in Arizona.

R14-6-201. Books and Records of Investment Advisers: requires investment advisers to comply with the provisions of the SEC's books and records rule; also requires the maintenance of certain additional records in separate files.

R14-6-202. Supervision: provides a safe harbor for investment advisers regarding their supervisory responsibilities by prescribing procedures for investment advisers to follow.

R14-6-203. Dishonest and Unethical Practices: provides guidance regarding which actions by investment advisers and investment adviser representatives will be construed to fall within the term "dishonest or unethical" for purposes of A.R.S. § 44-3201(A)(13).

R14-6-205. Information to be Furnished to Clients ("Brochure Rule"): prescribes information that must be furnished to clients and the timing and method of such disclosure.

R14-6-206. Custody of Client Funds or Securities by Investment Advisers: provides that it is a fraudulent practice under the IM Act for an investment adviser to fail to comply with the procedures prescribed in the Section when maintaining custody of a client's funds or securities.

R14-6-207. Suitability of Investment Advisory Services: provides that it is a fraudulent practice under the IM Act for an investment adviser to fail to provide suitable investment advice based on a reasonable inquiry of the client's financial situation, investment experience, and investment objectives.

R14-6-208. Advertisements by Investment Advisers or Investment Adviser Representatives: provides that it is a fraudulent practice under the IM Act for an investment adviser or investment adviser representative to fail to comply with the limitations on advertising and the requirements prescribed in the Section.

R14-6-209. Financial and Disciplinary Information that Investment Advisers Shall Disclose to Clients: provides that it is a fraudulent practice for an investment adviser to fail to disclose to any client or prospective client all material facts with respect to (1) a financial condition that is reasonably likely to impair the adviser's ability to meet contractual commitments to clients where the adviser has discretionary authority, custody, or requires prepayments of fees, (2) a legal or

disciplinary event that is material to the evaluation of the adviser's integrity or ability to meet contractual commitments to clients, or (3) a failure to comply with an arbitration award.

R14-6-210. Licensure of Investment Adviser Representatives: provides the circumstances under which investment adviser representatives who are employed by federally registered investment advisers must be licensed in Arizona. Also provides that a person employing investment adviser representatives who solicit on behalf of another investment adviser must license as an investment adviser.

R14-6-211. Solicitation: defines the activities that do not constitute solicitation for purposes of A.R.S. § 44-3101(3)(d).

R14-6-212. Filing Requirements: enumerates the specific filing requirements for licensure, notice filings, and renewal of licensure and notice filings.

7. A showing of good cause why the rules are necessary to promote a statewide interest if the rules will diminish a previous grant of authority of a political subdivision of this state:

Not applicable.

8. The summary of the economic, small business, and consumer impact:

The economic, small business, and consumer impact statement for the IM Rules analyzes the costs, savings, and benefits that accrue to the Commission, the office of the attorney general, the regulated public, and the general public. With the adoption of the proposed rules, the impact on established Commission procedures, Commission staff time, and other administrative costs is minimal. The estimated additional cost to the office of the attorney general is minimal. The benefits provided by the IM Rules are nonquantifiable. The IM Rules should benefit the Commission's relations with the regulated public because of increased uniformity with federal and other state laws, the addition of a provision for the

distribution of information regarding products and services on the Internet, the clarification of the statutory definition of investment adviser representative, the inclusion of parameters to the term "solicit" as used in the Arizona Investment Management Act adopted in April 1994 (the "IM Act"), and the clarification of filing requirements for licensure and notice filings. The public will benefit from the continuation of the licensing of, and imposition of standards on, persons providing financial services and the continued exclusion of nonqualified persons from the industry. The Commission anticipates that the proposed rulemaking may decrease and will not increase monitoring, record keeping, or reporting burdens on businesses or persons. The costs of implementation or enforcement are not increased or are only marginally increased and such increase does not equal or exceed the reduction in burdens.

9. A description of the changes between the proposed rules, including supplemental notices, and the final rules (if applicable):

To comply with format rules of the secretary of state, the Division has reformatted the capitalization of Section headings. In response to written comments, the Division has proposed changes to the text of several sections, which are not substantially different from the proposed rules. In addition, the Division has corrected a typographical error in 1 Section. These changes are set forth below and have been incorporated into the IM Rules attached to this Notice.

14-6-106(A)(1)(b): The investment adviser or investment adviser representative may only communicate with persons in Arizona individually about ~~effecting or attempting to effect transactions in services,~~ rendering investment advice for compensation, or solicit or negotiate ~~soliciting or negotiating~~ for the sale of investment advisory services if first compliant with or exempt from licensure or notice filing requirements.

14-6-106(A)(4): The Internet communication does not involve either ~~effecting or attempting to effect transactions in securities,~~ the rendering of investment advice for compensation, or individualized solicitation or negotiations for the sale of investment advisory services in Arizona.

14-6-106(B): Compliance with this Section relieves the investment adviser or investment adviser representative of licensure or notice filing requirements only. The investment adviser or investment adviser representative are is subject to Article 9 of the IM Act and related regulations.

14-6-203(A): ~~A. Except as otherwise provided in subsection (B), "dishonest"~~ "Dishonest and unethical practices," with respect to investment advisers and investment adviser representatives subject to under A.R.S. § 44-3201(A)(13), shall include but not be limited to the following:

14-6-203(B): ~~With respect to federal covered advisers, the provisions of this Section only apply to the extent the practice involves fraud or deceit and only to the extent permitted by Section 203A of the investment advisers act of 1940.~~

R14-6-206(B): With respect to federal covered advisers, the provisions of this Section only apply to the extent ~~the practice involves fraud or deceit and only to the extent permitted~~ by Section 203A of the Investment Advisers Act of 1940.

R14-6-207(B): With respect to federal covered advisers, the provisions of this Section only apply to the extent ~~the practice involves fraud or deceit and only to the extent permitted~~ by Section 203A of the Investment Advisers Act of 1940.

R14-6-208(D): With respect to federal covered advisers, the provisions of this Section only apply to the extent ~~the practice involves fraud or deceit and only to the extent permitted~~ by Section 203A of the Investment Advisers Act of 1940.

R14-6-209(F): With respect to federal covered advisers, the provisions of this Section only apply to the extent ~~the practice involves fraud or deceit and only to the extent permitted~~ by Section 203A of the Investment Advisers Act of 1940.

14-6-210(B)(1): (a) Immediately after entering into the investment advisory contract with the investment adviser has at least \$500,000 ~~\$750,000~~ under management with the investment adviser, or

(b) The investment adviser reasonably believes, immediately prior to entering into the advisory contract, has a net worth, together with assets held jointly with a spouse, at the time the contract is entered into of more than \$1,000,000 ~~\$1,500,000~~.

R14-6-212: Application, Notice Filing, and Renewal Filing Requirements

A. ~~In addition to the items enumerated in A.R.S. § 44-3153(B), a~~An application for licensure as an investment adviser under A.R.S. § 44-3153(B) shall include the following:

1. An original typewritten Form ADV with all information and exhibits required by the form.
2. An audited balance sheet if the investment adviser will have custody of client funds or if the investment adviser requires the payment of advisory fees six months or more in advance and in excess of \$500 for each client. The audited balance sheet shall be based on the investment adviser's fiscal year end, shall be prepared in accordance with generally accepted accounting principles, and shall be audited by

an independent certified public accountant. The notes to the balance sheet shall state the principles used to prepare the balance sheet, the basis of included securities, and any other explanation required for clarity.

13. A notarized affidavit of any officer, director, partner, member, trustee, or manager of the applicant stating:

- a. That a review of the records of the investment adviser has been conducted.
- b. Whether any investment adviser activity has been conducted with residents of Arizona prior to licensure as an investment adviser.

24. If the applicant intends to have a branch office in Arizona, the address and name of a contact individual located at such branch.

5. If part II of the Form ADV is not completed, the applicant shall submit a copy of the disclosure brochure the applicant gives or will give to clients.

6. The documents and fees required for each investment adviser representative as described in subsection (C).

7. The annual licensure fee required by A.R.S. § 44-3181(A).

B. A notice filing under A.R.S. § 44-3153(D) shall include the following: items enumerated in A.R.S. § 44-3153(D).

1. A manually signed and notarized Form ADV, part 1, page 1, or a copy of Form ADV, part 1, page 1, and an originally executed consent to service of process.

2. The documents and fees required for each investment adviser representative as described in subsection (C).

3. The annual notice filing fee required by A.R.S. § 44-3181(A).

C. An application for an investment adviser representative licensure under A.R.S. § 44-3156 shall include the following:

1. A complete Form U-4.
2. Proof of successful completion of required examinations in accordance with A.A.C. R14-6-204.
3. The annual licensure fee required by A.R.S. § 44-3181(A).

CD. For purposes of A.R.S. § 44-3158(A), a license of an investment adviser or an investment adviser representative shall be renewed upon receipt of the nonrefundable license fee prescribed in A.R.S. § 44-3181.

DE. For purposes of A.R.S. § 44-3153(E), a notice filing shall be renewed upon receipt of the nonrefundable license fee prescribed in A.R.S. § 44-3181.

10. A summary of the principal comments and the agency response to them:

The agency received six comments letters following the Notice of Proposed Rulemaking from the following organizations: the Investment Counsel Association of America, Inc. ("ICAA"); the Certified Financial Planner Board of Standards ("CFP"); the Institute of Certified Financial Planners ("ICFP"); Benchmark Financial, Ltd. ("BFL"); a BFL follow-up letter; and a further BFL letter to which was attached a copy of the ICFP's comments.

Comments addressed the following:

R14-6-106 ("rule 106") provides that the general dissemination of information on the internet by investment advisers and investment adviser representatives shall not be deemed transacting business in Arizona based solely on that activity if the conditions contained in rule 106 are observed. The ICFP recommended 3 changes as follows: that the Commission include the term "federal covered adviser" in Rule 106 to clarify that it applies to both state

and federally registered investment advisers; that the Commission delete the prohibition from effecting transactions in securities contained in rule 106(A)(1)(b) and 106(A)(4) because an adviser cannot execute a securities transaction under the IMA; and that the Commission include in subsection (A)(4) the phrase "unless the investment adviser or investment adviser representative is compliant with or exempt from licensure or notice filing requirements" so that investment advisers are not precluded from relying on the de minimus exemption.

Regarding the ICFP's first recommendation, the Commission made no change because the use of the terms "investment advisers" and "investment adviser representatives" to refer to all persons that fall within the statutory definition, whether federally registered or state licensed, is consistent with the use throughout the IM Act and IM Rules.

Regarding ICFP's second recommendation, the Commission revised rule 106 in accordance with the recommendation.

Regarding ICFP's third recommendation, the Commission made no change because rule 106 does not preclude a person from relying on the de minimus exemption.

R14-6-201 identifies the books and record keeping requirements. ICAA recommended that the Commission use the model language of the North American Securities Administrators Association ("NASAA") because the model language was less ambiguous. The Commission did not agree and made no change.

R14-6-203 ("rule 203") enumerates practices that are dishonest and unethical under A.R.S. § 44-3201(A)(13), which provides for the denial, revocation, or suspension of the license of an investment adviser or investment adviser representative.

The ICAA recommended that investment adviser representatives of federal covered advisers be precluded from the application of rule 203. The Commission deleted subsection

(B) from rule 203. The Commission did not preclude from the scope of the rule investment adviser representatives of federally registered investment advisers because the Securities and Exchange Commission ("SEC") does not register or regulate investment adviser representatives, allocating the regulation of investment adviser representatives to the states in which the representatives do business. The Investment Advisers Act of 1940, section 203A(b)(1)(A), explicitly states that "a State may license, register or otherwise qualify any investment adviser representative who has a place of business located within that State." All investment adviser representatives who are licensed in Arizona are and should be subject to statutory and rule provisions under which those licenses may be denied, suspended, or revoked.

R14-6-204 ("rule 204") prescribes examination requirements for individual investment advisers and investment adviser representatives for licensure in Arizona. The ICFP and the CFP supported the adoption by Arizona of a new series 65 examination being prepared, but not yet finalized at the time of the Notice of Proposed Rulemaking, by NASAA. On July 23, 1999, the Commission published a Notice of Termination of Rulemaking regarding rule 204 and initiated a separate rulemaking package.

R14-6-206 ("rule 206"), R14-6-207 ("rule 207"), R14-6-208 ("rule 208"), and R14-6-209 ("rule 209") enumerate activities that constitute a fraudulent practice within the meaning of A.R.S. § 44-3241(A)(4), which states it is a fraudulent practice and unlawful to engage in any transaction, practice, or course of business that operates or would operate as a fraud or deceit.

The ICAA recommended that federally registered investment advisers and their investment adviser representatives be excluded from the application of rules 206 through

209. The Commission did not exclude investment adviser representatives of federally registered investment advisers from rules 206 through 209 because the SEC has allocated regulation of investment adviser representative to states.

The Commission did not exclude federally registered investment advisers from the rules because each proposed rule contains a provision that limits the application of the rule to the extent permitted by section 203A of the Investment Advisers Act of 1940. The Commission did simplify the provision, which is contained in subsections (B) of rules 206 and 207, subsection (D) of rule 208, and subsection (F) in rule 209.

The ICFP requested that the Commission include a safe harbor in rule 206 that would allow an investment adviser to accept third-party checks and endorsed stock certificates to forward to other persons as a service to its clients without being deemed to have custody of the checks and stock certificates. Rule 206 is modeled after federal rule 206(4)-2 promulgated under the Investment Advisers Act of 1940. The Commission understands that ICFP also has requested that the SEC include such a safe harbor in federal rule 206(4)-2 and that the SEC has taken the matter under advisement.

Because the Commission is not aware of any situation where interpretations of custody have caused investment advisers problems with regulators, the Commission has elected not to respond to the ICFP request prior to SEC action on the issue.

R14-6-210 ("rule 210") defines investment adviser representative based on the definition contained in federal rule 203A-3 and the NASAA model language. The ICFP and ICAA commented that federal rule 205-3, referenced in federal rule 203A-3, has been amended. The Commission revised rule 210 to reflect that amendment.

R14-6-212 ("rule 212") enumerates the filing requirements for licensure, notice filings, and renewals. ICAA requested that the filing requirements be listed with greater specificity and the Commission revised rule 212 as requested.

11. Any other matters prescribed by statute that are applicable to the specific agency or to any specific rule or class of rules:

None.

12. Incorporations by reference and their location in the rules:

17 CFR 275.204.2 (1998) A.A.C. R14-6-101(B)(16)

13. Whether the rule was previously adopted as an emergency rule and, if so, whether the text was changed between adoption as an emergency rule and the adoption of the final rule.

Not applicable.

14. The full text of the rule follows:

TITLE 14. PUBLIC SERVICE CORPORATIONS, CORPORATIONS

AND ASSOCIATIONS; SECURITIES REGULATION

CHAPTER 6. CORPORATION COMMISSION--INVESTMENT MANAGEMENT

ARTICLE 1. GENERAL PROVISIONS RELATING TO THE ARIZONA

INVESTMENT MANAGEMENT ACT

~~R14-6-101. Definitions~~

R14-6-101. Definitions

~~R14-6-102. Scope of Rules~~

R14-6-102. Scope of Provisions

~~R14-6-103 Severability~~

R14-6-103 Severability

~~R14-6-104 Enforcement of the Arizona Investment Management Act~~

R14-6-104 Enforcement of the Arizona Investment Management Act

R14-6-106 General Dissemination of Information on the Internet

ARTICLE 2. DUTIES OF INVESTMENT ADVISERS AND

INVESTMENT ADVISER REPRESENTATIVES

~~R14-6-201. Books and Records of Investment Advisers~~

R14-6-201. Books and Records of Investment Advisers

~~R14-6-202. Supervision~~

R14-6-202. Supervision

~~R14-6-203. Dishonest and Unethical Practices~~

R14-6-203. Dishonest and Unethical Practices

~~R14-6-205. Information to be Furnished to Clients ("Brochure Rule")~~

R14-6-205. Information to be Furnished to Clients ("Brochure Rule")

~~R14-6-206. Custody of Client Funds or Securities by Investment Advisors~~

R14-6-206. Custody of Client Funds or Securities by Investment Advisors

~~R14-6-207. Suitability of Investment Advisory Services~~

R14-6-207. Suitability of Investment Advisory Services

~~R14-6-208. Advertisements by Investment Advisors or Investment Adviser Representatives~~

R14-6-208. Advertisements by Investment Advisors or Investment Adviser Representatives

~~R14-6-209. Financial and Disciplinary Information that Investment Advisors Must Disclose to
Clients~~

R14-6-209. Financial and Disciplinary Information that Investment Advisors Shall Disclose to
Clients

R14-6-210. Licensure of Investment Adviser Representatives

R14-6-211. Solicitation

R14-6-212. Application, Notice Filing, and Renewal Requirements

ARTICLE 1. GENERAL PROVISIONS RELATING TO THE ARIZONA
INVESTMENT MANAGEMENT ACT

~~R14-6-101. Definitions~~

~~A.—The definitions set forth in A.R.S. §§ 44-1801 and 44-3101 shall apply to the rules promulgated under Chapter 13.~~

~~B.—The following definitions shall apply to all rules promulgated under Chapter 13 unless the context otherwise requires:~~

~~1.—“IM Act” means the Arizona Investment Management Act, A.R.S. § 44-3101 et seq.~~

~~2.—“Advertisement” means, except as set forth in subsections (d) and (e), any notice, circular, letter, or other written, oral, or electronically generated communication addressed to or reasonably designed by the investment adviser or investment adviser representative to be accessed by more than 1 person, or any notice or other announcement in any publication or by radio or television, which directly or indirectly offers:~~

~~a.—Any analysis, report, or publication concerning securities, or which is to be used in making any determination as to when to buy or sell any security, or which security to buy or sell; or~~

~~b.—Any graph, chart, formula, or other device to be used in making any determination as to when to buy or sell any security, or which security to buy or sell; or~~

~~c.—Any other investment advisory service with regard to securities; or~~

~~d.—A communication over a computer on-line service including, but not limited to, an electronic bulletin board shall not be deemed to be an advertisement when an investment adviser or an investment adviser representative is either:~~

- ~~i. Engaged in a discussion regarding securities and does not receive compensation from any person for the discussion; or~~
 - ~~ii. Responds to unsolicited inquiries regarding the provision of investment advisory services.~~
- ~~e. A communication by 1 or more investment advisers or investment adviser representatives shall not be deemed to be an advertisement when the communication is addressed solely to or is reasonably designed to be accessed solely by other investment advisers or investment adviser representatives.~~
- ~~3. "Certified public accountant" or "CPA" means an accountant who has been registered or licensed to practice public accounting and is permitted to use the title "certified public accountant" and use the initials "CPA" after the accountant's name.~~
- ~~4. "Chapter 13" means A.R.S. Title 44, Chapter 13.~~
- ~~5. "Commodity Exchange Act" means 7 U.S.C. 1 *et seq.* (1988 & Supp. V 1993), which is incorporated by reference, does not contain any later amendments or editions, and is on file in the Office of the Secretary of State. Copies of the Commodity Exchange Act are available from the Securities Division of the Corporation Commission and from the Superintendent of Documents, Government Printing Office, Washington, D.C. 20402.~~
- ~~6. "Division" means the Securities Division of the Corporation Commission.~~
- ~~7. "Fixed fee basis" means an investment advisory fee which at any given time can be precisely established in dollar amount without regard to the investment performance or value of an account and which is not based on the purchase or sale of specific securities.~~
- ~~8. "Form ADV" means the Uniform Application for Investment Adviser Registration, 17 CFR 279.1 (1994) (Form amended at 59 FR 21657 (1994) and 59 FR 27659 (1994)),~~

~~which is incorporated by reference, does not contain any later amendments or editions, and is on file in the Office of the Secretary of State. Copies of Form ADV are available from the Division and from the Superintendent of Documents, Government Printing Office, Washington, D.C. 20402.~~

9. ~~“Impersonal advisory services” means investment advisory services provided solely:~~
- ~~a. By means of written material or oral statements that do not purport to meet the objectives or needs of specific individuals or accounts;~~
 - ~~b. Through the issuance of statistical information containing no expression of opinion as to the investment merits of a particular security; or~~
 - ~~c. Any combination of the foregoing services.~~
10. ~~“NASAA” means the North American Securities Administrators Association, Inc. or any successor organization.~~
11. ~~“NASD” means the National Association of Securities Dealers, Inc. or any successor organization.~~
12. ~~“Relative” means any relationship by blood, marriage, or adoption, not more remote than 1st cousin.~~
13. ~~“Rule 204-2” means United States Securities and Exchange Commission Rule 204-2, 17 CFR 275.204.2 (1994), which is incorporated by reference, does not contain any later amendments or editions, and is on file in the Office of the Secretary of State. Copies of Rule 204-2 are available from the Division and from the Superintendent of Documents, Government Printing Office, Washington, D.C. 20402.~~
14. ~~“Rule 204-3” means United States Securities and Exchange Commission Rule 204-3, 59 FR 21661 (1994) (to be codified at 17 CFR 275.204.3), which is incorporated by~~

~~reference, does not contain any later amendments or editions, and is on file in the Office of the Secretary of State. Copies of Rule 204-3 are available from the Division and from the Superintendent of Documents, Government Printing Office, Washington, D.C. 20402.~~

~~15. "SEC" means United States Securities and Exchange Commission.~~

~~16. "Securities Act" means the Securities Act of Arizona, A.R.S. § 44-1801 et seq.~~

~~17. "Unincorporated organization" includes a limited liability company for purposes of the definition of "person," as defined in A.R.S. § 44-1801(13).~~

R14-6-101. Definitions

- A. The definitions set forth in A.R.S. §§ 44-1801 and 44-3101 shall apply to the rules promulgated under A.R.S. Title 44, Chapter 13.
- B. The following definitions shall apply to all rules promulgated under A.R.S. Title 44, Chapter 13, unless the context otherwise requires:
 - 1. "Advertisement" means, except as set forth in subsections (d) and (e), any notice, circular, letter, or other written, oral, or electronically generated communication addressed to or reasonably designed by the investment adviser or investment adviser representative to be accessed by more than 1 person, or any notice or other announcement in any publication or by radio or television, that directly or indirectly offers:
 - a. Any analysis, report, or publication that either concerns securities, or is to be used in making any determination as to when to buy or sell any security or which security to buy or sell; or

- b. Any graph, chart, formula, or other device to be used in making any determination as to when to buy or sell any security, or which security to buy or sell; or
 - c. Any other investment advisory service with regard to securities; or
 - d. A communication over a computer on-line service including but not limited to an electronic bulletin board shall not be deemed to be an advertisement when an investment adviser or an investment adviser representative is either:
 - i. Engaged in a discussion regarding securities and does not receive compensation from any person for the discussion; or
 - ii. Responds to unsolicited inquiries regarding the provision of investment advisory services.
 - e. A communication by 1 or more investment advisers or investment adviser representatives shall not be deemed to be an advertisement when the communication is addressed solely to or is reasonably designed to be accessed solely by other investment advisers or investment adviser representatives.
2. "Certified public accountant" or "CPA" means an accountant who has been registered or licensed to practice public accounting and is permitted to use the title "certified public accountant" and to use the initials "CPA" after the accountant's name.
3. "Federal covered adviser" means an investment adviser registered under the Investment Advisers Act of 1940.
4. "Fixed fee basis" means an investment advisory fee that at any given time can be precisely established in a dollar amount without regard to the investment performance or value of an account and that is not based on the purchase or sale of specific securities.

5. "Form ADV" means the Uniform Application for Investment Adviser Registration, 17 CFR 279.1.
6. "IM Act" means the Arizona Investment Management Act, A.R.S. § 44-3101 *et seq.*
7. "Impersonal advisory services" means investment advisory services provided solely:
 - a. By means of written material or oral statements that do not purport to meet the objectives or needs of specific individuals or accounts;
 - b. Through the issuance of statistical information containing no expression of opinion as to the investment merits of a particular security; or
 - c. Any combination of the foregoing services.
8. "Internet" means all proprietary or common carrier electronic systems, or similar media.
9. "Internet communication" means the distribution of information on the Internet.
10. "Investment-related" means pertaining to securities, commodities, banking, insurance, or real estate, including but not limited to acting as or being associated with a broker-dealer, investment company, investment adviser, government securities broker or dealer, municipal securities dealer, bank, savings and loan association, entity, or person required to be registered under the Commodity Exchange Act, or fiduciary.
11. "Involved" means acting or aiding, abetting, causing, counseling, commanding, inducing, conspiring with, or failing reasonably to supervise another in doing an act.
12. "Management person" means a person with power to exercise, directly or indirectly, a controlling influence over the management or policies of an investment adviser that is a company or to determine the general investment advice given to clients.
13. "NASAA" means the North American Securities Administrators Association, Inc., or any successor organization.

14. "NASD" means the National Association of Securities Dealers, Inc., or any successor or subsidiary organization.
15. "Relative" means any relationship by blood, marriage, or adoption, not more remote than 1st cousin.
16. "Rule 204-2" means United States securities and exchange commission rule 204-2, 17 CFR 275.204-2 (1998), which is incorporated by reference, does not contain any later amendments or editions, and is on file in the office of the secretary of state. Copies of Rule 204-2 are available from the Division and from the Superintendent of Documents, Government Printing Office, Washington, D.C. 20402.
17. "SEC" means United States Securities and Exchange Commission.
18. "Securities Act" means the Securities Act of Arizona, A.R.S. § 44-1801 *et seq.*
19. "Self-regulatory organization" or "SRO" means any national securities or commodities exchange, registered association, or registered clearing agency.
20. "Unincorporated organization" includes a limited liability company for purposes of the definition of "person," as defined in A.R.S. § 44-1801.
21. "Wrap fee program" means a program under which any client is charged a specified fee or fees not based directly upon transactions in a client's account for investment advisory services, which may include portfolio management or advice concerning the selection of other investment advisers, and execution of client transactions.

~~R14-6-102. — Scope of this Article~~

~~The following rules are adopted by the Commission under the authority granted pursuant to Chapter 13. All rules shall be generally applicable to the administration of the IM Act but the Commission may at any time abrogate or waive strict adherence to any particular rule in any~~

~~specific instance where the Commission may deem it advisable for the equitable administration of the law. When not in conflict with these rules, the applicable provisions of A.A.C. R14-3-101 through R14-3-113 also shall apply.~~

R14-6-102. Scope of Provisions

The following Sections are adopted by the Commission under the authority granted pursuant to A.R.S. Title 44, Chapter 13. Such Sections shall be generally applicable to the administration of the IM Act, but the Commission may at any time abrogate or waive strict adherence to any particular provision when the Commission deems it advisable for the equitable administration of the law. When not in conflict with these Sections, the applicable provisions of A.A.C. R14-3-101 through R14-3-113 also shall apply.

~~R14-6-103. Severability~~

~~The provisions of the rules promulgated under Chapter 13 are severable. If any provision of a rule is held to be invalid, such invalidity shall not affect other provisions which can be given effect without the invalid provision.~~

R14-6-103. Severability

The provisions of the Sections promulgated under A.R.S. Title 44, Chapter 13, are severable. If any provision of a Section is held to be invalid, such invalidity shall not affect other provisions that can be given effect without the invalid provision.

~~R14-6-104. Enforcement of the Arizona Investment Management Act~~

~~The rules relating to investigations and examinations conducted pursuant to and orders issued under the IM Act are contained at A.A.C. R14-4-301 through R14-4-308.~~

R14-6-104. Enforcement of the Arizona Investment Management Act

The provisions relating to investigations and examinations conducted pursuant to and orders issued under the IM Act are contained at A.A.C. R14-4-301 through R14-4-308.

R14-6-106. General Dissemination of Information on the Internet

A. Investment advisers and investment adviser representatives who use the Internet to distribute information on products and services directed generally to anyone having access to the Internet shall not be deemed to be transacting business in Arizona for purposes of Article 4 of the IM Act based solely on that activity if the following conditions are observed:

1. The Internet communication includes clear and prominent statements that:
 - a. The investment adviser or investment adviser representative may only transact business in Arizona if first compliant with or exempt from licensure or notice filing requirements.
 - b. The investment adviser or investment adviser representative may only communicate with persons in Arizona individually about rendering investment advice for compensation or solicit or negotiate for the sale of investment advisory services if first compliant with or exempt from licensure or notice filing requirements.
2. The investment adviser or investment adviser representative complies with the statements contained in the Internet communication under subsection (A)(1).
3. The Internet communication is subject to a mechanism, policy, or procedure reasonably designed to ensure that, prior to any subsequent, direct communication with prospective customers or clients in Arizona, the investment adviser or investment adviser

representative is first compliant with or exempt from the licensure or notice filing requirements of the IM Act.

4. The Internet communication does not involve either the rendering of investment advice for compensation or individualized solicitation or negotiations for the sale of investment advisory services in Arizona.
 5. In the case of an investment adviser representative:
 - a. The affiliation with an investment adviser is prominently disclosed in the Internet communication.
 - b. The investment adviser with whom the investment adviser representative is associated first authorizes the Internet communication.
 - c. The investment adviser with whom the investment adviser representative is associated retains responsibility for reviewing and approving the content of any Internet communication.
 - d. In distributing information through the Internet, the investment adviser representative acts within the scope of the authority granted by the investment adviser.
- B. Compliance with this Section relieves the investment adviser or investment adviser representative of licensure or notice filing requirements only. The investment adviser or investment adviser representative is subject to Article 9 of the IM Act and related regulations.

ARTICLE 2. DUTIES OF INVESTMENT ADVISERS AND
INVESTMENT ADVISER REPRESENTATIVES

~~R14-6-201. Books and Records of Investment Advisers~~

- ~~A. Each investment adviser shall make, maintain, and preserve books and records in compliance with Rule 204-2. The investment adviser shall concurrently file with the Commission a copy of any notices or written undertakings required to be filed with the SEC under Rule 204-2.~~
- ~~B. To the extent that the SEC amends Rule 204-2, investment advisers in compliance with Rule 204-2 as amended shall not be deemed to be in violation of this Section and shall not be subject to enforcement action by the Commission for violation of this Section to the extent that the violation results solely from the investment adviser's compliance with the amended Rule 204-2.~~
- ~~C. As of the effective date of this Section, each investment adviser shall make, maintain, and preserve for at least 5 years the following additional books and records:~~
- ~~1. A file containing each customer complaint received relating to advisory activities conducted by the investment adviser, its investment advisory representatives, or its employees, and all correspondence relating to such complaint;~~
 - ~~2. A file containing all advertisements used by the investment adviser or any investment adviser representative, including any radio or television transcripts and advertisements placed on computer or electronic bulletin boards;~~
 - ~~3. In each client file, all correspondence received or sent by the investment adviser, any investment adviser representative, or any employee, that relates to any client account, securities, or funds.~~

~~D. Books and records that are required to be maintained pursuant to subsection (A) shall be available for inspection by the Commission in accordance with the provisions of Rule 204-2. Books and records that are required to be maintained pursuant to subsection (C) shall be readily accessible and may be preserved in accordance with Rule 204-2(g).~~

R14-6-201. Books and Records of Investment Advisers

- A. Except as provided in subsection (G), each investment adviser licensed or required to be licensed under the IM Act shall make, maintain, and preserve books and records in accordance with the requirements imposed on federal covered advisers under rule 204-2. The investment adviser shall file with the Commission a copy of any notices or written undertakings required to be filed by federal covered advisers with the SEC under rule 204-2.
- B. To the extent that the SEC amends rule 204-2, investment advisers in compliance with the requirements contained in rule 204-2 as amended shall not be deemed to be in violation of this Section and shall not be subject to enforcement action by the Commission for violation of this Section to the extent that the violation results solely from the investment adviser's compliance with the requirements contained in the amended rule 204-2.
- C. Except as provided in subsection (G), each investment adviser licensed or required to be licensed under the IM Act shall make, maintain, and preserve for at least 5 years the following additional books and records:
1. A file containing each customer complaint received relating to advisory activities conducted by the investment adviser, its investment advisory representatives, or its employees, and all correspondence relating to such complaint.

2. A file containing all advertisements used by the investment adviser or any investment adviser representative, including any radio or television transcripts and advertisements placed on computer or electronic bulletin boards.
 3. In each client file, all correspondence received or sent by the investment adviser, any investment adviser representative, or any employee, that related to any client account, securities, or funds.
- D. Books and records that are required to be maintained pursuant to subsection (A) shall be available for inspection by the Commission in accordance with the provisions of rule 204-2. Books and records that are required to be maintained pursuant to subsection (C) shall be readily accessible and may be preserved in accordance with rule 204-2(g). Notwithstanding other record preservation requirements of this Section, the following records or copies shall be maintained at the business location of the investment adviser from which the customer or client is being provided or has been provided with investment advisory services:
1. Records required to be preserved under rule 204-2(a)(3), (a)(7) through (10), (a) (14) through (15), (b), and (c).
 2. Records required to be preserved under subsection (C) of this Section.
- E. A record made and kept under a provision of subsections (A) or (C) that contains all of the information required under any other provision of subsections (A) or (C) in a readily accessible format need not be maintained in duplicate in order to meet the requirements of the other provision.
- F. Any book or other record made, kept, maintained, and preserved in compliance with A.A.C. R14-4-132 that is substantially the same as the book or other record required to be made,

kept, maintained, and preserved under this Section shall be deemed to be made, kept, maintained, and preserved in compliance with this Section.

- G. Every investment adviser licensed or required to be licensed in Arizona that has its principal place of business in a state other than Arizona shall be exempt from the requirements of this Section, provided the investment adviser is licensed in such other state and is in compliance with that state's recordkeeping requirements.

~~R14-6-202. Supervision~~

~~For purposes of A.R.S. § 44-3201(A)(12), no investment adviser shall be deemed to have failed to reasonably supervise its investment adviser representatives or employees if:~~

- ~~1. There have been established and maintained written procedures, and a system for applying such procedures, which would reasonably be expected to prevent and detect, insofar as practicable, any violation by such investment adviser representatives or employees of the IM Act, or any rule adopted thereunder; and~~
- ~~2. Such investment adviser has reasonably discharged the duties and obligations incumbent upon it by reason of such procedures and system without reasonable cause to believe that such procedures and system were not being complied with.~~

R14-6-202. Supervision

For purposes of A.R.S. § 44-3201(A)(12), no investment adviser shall be deemed to have failed to reasonably supervise its investment adviser representatives or employees if:

1. The investment adviser has established and maintained written procedures, and a system for applying such procedures, that reasonably may be expected to prevent and detect, insofar as practicable, any violation of the IM Act or any rule adopted thereunder by such investment adviser representatives or employees; and

2. Such investment adviser has discharged reasonably the duties and obligations incumbent upon it by reason of such procedures and system without reasonable cause to believe that the investment adviser representatives or employees are not complying with such procedures and system.

~~R14-6-203. Dishonest and Unethical Practices~~

~~"Dishonest and unethical practices", with respect to investment advisers and investment adviser representatives under A.R.S. § 44-3201(A)(13) shall include, but not be limited to, the following:~~

- ~~1. Refusing to allow or otherwise impeding designees of the Commission from conducting an investigation or examination under the IM Act or any rule adopted thereunder;~~
- ~~2. Placing an order to purchase or sell a security for the account of a client without authority to do so;~~
- ~~3. Placing an order to purchase or sell a security for the account of a client upon instruction of a 3rd party without first obtaining a written 3rd party trading authorization from the client;~~
- ~~4. Exercising any discretionary power in placing an order for the purchase or sale of securities for a client without first obtaining written discretionary authority, unless the discretionary power relates solely to the price at which, or the time when, an order involving a definite amount of specified securities shall be executed, or both;~~
- ~~5. Inducing trading in a client's account that is excessive in size or frequency in view of the financial resources, investment objectives, and character of the account;~~
- ~~6. Borrowing money or securities from a client or client's account unless the client is a dealer, an affiliate, or relative of the investment adviser or investment adviser~~

~~representative, or a financial institution or other entity engaged in the business of
loaning funds or securities;~~

- ~~7. Lending money to a client unless the investment adviser or investment adviser
representative is a financial institution or other entity engaged in the business of loaning
funds or the client is an affiliate or relative of the investment adviser or investment
adviser representative;~~
- ~~8. Misrepresenting to any client, or prospective client, the qualifications of the investment
adviser, the investment adviser representative, or an employee, or misrepresenting the
nature of the investment advisory services being offered or fees to be charged for such
services, or omitting to state a material fact necessary to make the statements made
regarding qualifications, services, or fees, in light of the circumstances under which they
were made, not misleading;~~
- ~~9. Providing a report or recommendation to any client prepared by someone other than the
investment adviser or investment adviser representative without disclosing that fact.
This prohibition does not apply to a situation where the investment adviser or
investment adviser representative uses published research reports or statistical analyses
to render investment advice or where the investment adviser or investment adviser
representative orders such a report in the ordinary course of providing service;~~
- ~~10. Charging a client an investment advisory fee that is unreasonable in light of the type of
services to be provided, the experience and expertise of the investment adviser or the
investment adviser representative, the sophistication and bargaining power of the client,
and whether the investment adviser has disclosed that lower fees for comparable
services may be available from other sources;~~

- ~~11. Failing to disclose to a client in writing before entering into or renewing an investment advisory agreement with that client, or before any investment advice is rendered, any material conflict of interest relating to the investment adviser, the investment adviser representative, or an employee which could reasonably be expected to impair the rendering of unbiased and objective advice including, but not limited to:~~
- ~~a. Compensation arrangements connected with investment advisory services to clients which are in addition to compensation from such clients for those services; and~~
 - ~~b. Charging a client an investment advisory fee for rendering investment advice without disclosing that compensation for executing securities transactions pursuant to such investment advice will be received by the investment adviser, the investment adviser representative, or an employee;~~
- ~~12. Promising or guaranteeing a client that a gain, loss, or other outcome will be achieved as a result of the investment advice;~~
- ~~13. Disclosing the identity, affairs, or investments of a client to any 3rd party unless required by law to do so, or unless consented to by the client;~~
- ~~14. With respect to any client initially retained after the effective date of this rule, entering into, extending, modifying, or renewing any investment advisory contract except a contract for impersonal advisory services unless such contract is in writing and discloses all the material terms of the contract including but not limited to the services to be provided, the investment advisory fee or the formula for computing the fee, the amount or the manner of calculation of the amount of the prepaid fee to be returned in the event of contract termination or non-performance, and of any grant of discretionary power to the investment adviser;~~

- ~~15. With respect to any client initially retained after the effective date of this rule, entering into, extending, modifying, or renewing any investment advisory contract without disclosing, in writing to the client, any affirmative answers to disciplinary questions numbered 11A and 11K in Part I of the Form ADV;~~
- ~~16. Entering into, extending, modifying, or renewing any investment advisory contract which allows the assignment of such contract by the investment adviser without the prior written consent of the client;~~
- ~~17. Committing any act that results in denial, revocation, or suspension of a license or registration relating to securities by an agency of any state, where such denial, revocation or suspension arises out of any scheme, act, practice or course of business that operates or would operate as a fraud or deceit, or arises out of a violation of Article 13 of the Securities Act or the rules promulgated thereunder; and~~
- ~~18. For any investment adviser to, in any manner, request, or require, in any contract, agreement, or otherwise, any condition, stipulation, or provision binding on any person to waive compliance with any provision of the IM Act or the rules thereunder. Any such waiver shall be void.~~

R14-6-203. Dishonest and Unethical Practices

“Dishonest and unethical practices,” with respect to investment advisers and investment adviser representatives subject to A.R.S. § 44-3201(A)(13), shall include but not be limited to the following:

1. Refusing to allow or otherwise impeding the Commission from conducting an investigation or examination under the IM Act or any rule adopted thereunder.

2. Placing an order to purchase or sell a security for the account of a client without authority to do so.
3. Placing an order to purchase or sell a security for the account of a client upon instruction of a 3rd party without first obtaining a written 3rd-party trading authorization from the client.
4. Exercising any discretionary power in placing an order for the purchase or sale of securities for a client without first obtaining written discretionary authority, unless the discretionary power relates solely to the price at which, or the time when, an order involving a definite amount of specified securities shall be executed, or both.
5. Inducing trading in a client's account that is excessive in size or frequency in view of the financial resources, investment objectives, and character of the account.
6. Borrowing money or securities from a client or client's account unless the client has authorized the borrowing in writing and is a dealer, an affiliate, or relative of the investment adviser or investment adviser representative, or a financial institution or other entity engaged in the business of loaning funds or securities.
7. Loaning money to a client unless the investment adviser or investment adviser representative is a financial institution or other entity engaged in the business of loaning funds or the client is an affiliate or relative of the investment adviser or investment adviser representative.
8. Misrepresenting to any client, or prospective client, the qualifications of the investment adviser, the investment adviser representative, or an employee, or misrepresenting the nature of the investment advisory services being offered or fees to be charged for such services, or omitting to state a material fact necessary to make the statements made

regarding qualifications, services, or fees, in light of the circumstances under which they were made, not misleading.

9. Providing a report or recommendation to any client prepared by someone other than the investment adviser or investment adviser representative without disclosing that fact.

This prohibition does not apply to a situation where the investment adviser or investment adviser representative uses published research reports or statistical analyses to render investment advice or where the investment adviser or investment adviser representative orders such a report in the ordinary course of providing service.

10. Charging a client an investment advisory fee that is unreasonable in light of the type of services to be provided, the experience and expertise of the investment adviser or the investment adviser representative, and the sophistication and bargaining power of the client.

11. Failing to disclose to a client in writing before entering into or renewing an investment advisory agreement with that client, or before any investment advice is rendered, any material conflict of interest relating to the investment adviser, the investment adviser representative, or an employee that could reasonably be expected to impair the rendering of unbiased and objective advice including but not limited to:

- a. Compensation arrangements connected with investment advisory services to clients that are in addition to compensation from such clients for those services; and
- b. Charging a client an investment advisory fee for rendering investment advice without disclosing that compensation for executing securities transactions pursuant to such investment advice will be received by the investment adviser, the investment adviser representative, or an employee.

12. Guaranteeing a client that a gain, loss, or other outcome will be achieved as a result of the investment advice.
13. Disclosing the identity, affairs, or investments of a client to any 3rd party unless required by law to do so or consented to by the client.
14. With respect to any client initially retained after July 19, 1996, entering into, extending, modifying, or renewing any investment advisory contract except a contract for impersonal advisory services unless such contract is in writing and discloses all the material terms of the contract including but not limited to the services to be provided, the investment advisory fee or the formula for computing the fee, the amount or the manner of calculation of the amount of the prepaid fee to be returned in the event of contract termination or nonperformance, and that grant of any discretionary power to the investment adviser.
15. With respect to any client initially retained after July 19, 1996, entering into, extending, modifying, or renewing any investment advisory contract without disclosing, in writing to the client, any affirmative answers to disciplinary questions numbered 11A and 11K in Part I of the Form ADV.
16. Entering into, extending, modifying, or renewing any investment advisory contract that allows the assignment of such contract by the investment adviser without the prior written consent of the client.
17. Committing any act that results in denial, revocation, or suspension by an agency of any state of a license or registration relating to securities, where such denial, revocation, or suspension arises out of any scheme, act, practice, or course of business that operates or

would operate as fraud or deceit, or arises out of a violation of Article 13 of the Securities Act or the rules promulgated thereunder.

18. Failing to comply with any arbitration award issued in connection with doing business as an investment adviser or investment adviser representative or as a dealer or salesman as defined in A.R.S. Title 44, Chapter 12.

19. Requesting or requiring any person to waive compliance with any provision of the IM Act or the rules thereunder. Any such waiver shall be void.

~~R14-6-205. Information to be Furnished to Clients ("Brochure Rule")~~

~~A. Each investment adviser shall comply with the provisions of Rule 204-3.~~

~~B. To the extent that the SEC amends Rule 204-3, investment advisers in compliance with Rule 204-3 as amended shall not be deemed to be in violation of this Section and shall not be subject to enforcement action by the Commission for violation of this Section to the extent that the violation results solely from the investment adviser's compliance with the amended Rule 204-3.~~

R14-6-205. Information to be Furnished to Clients ("Brochure Rule")

A. Each investment adviser licensed or required to be licensed under the IM Act shall furnish each client and prospective client with a written disclosure statement that may be either a copy of Part II of its Form ADV or a written document containing at least the information required by Part II of Form ADV.

B. The information required to be disclosed by subsection (A) shall be disclosed to clients not less than 48 hours prior to entering into any written or oral investment advisory contract, or no later than the time of entering into such contract if the client has the right to terminate the contract without penalty within 5 business days after entering into the contract.

- C. An investment adviser need not deliver the statement required by subsection (A) in connection with entering into an investment company contract or a contract for impersonal advisory services. The investment adviser shall, however, offer in writing to deliver the statement within 7 business days upon receipt of a written request.
- D. Without charge and to each of its clients, an investment adviser licensed or required to be licensed under the IM Act shall deliver annually within 7 business days upon receipt of a written request or offer in writing to deliver the statement required by this Section.
- E. If an investment adviser licensed or required to be licensed under the IM Act renders substantially different types of investment advisory services to different clients, any information required by Part II of Form ADV may be omitted from the statement furnished to the client or prospective client if such information is applicable only to a type of investment advisory service or fee that is not rendered or charged, or proposed to be rendered or charged, to that client or prospective client.
- F. Nothing in this Section shall relieve any investment adviser from any obligation pursuant to any provision of the IM Act or the rules and regulations thereunder or other federal or state law to disclose any information to its clients or prospective clients not specifically required by this Section.
- G. An investment adviser licensed or required to be licensed under the IM Act that is compensated under a wrap fee program for sponsoring, organizing, or administering the program, or for selecting, or providing advice to clients regarding the selection of, other investment advisers in the programs, shall, in lieu of the written disclosure statement required by subsection (A) and in accordance with the other subsections of this Section, furnish each client and prospective client of the wrap fee program with a written disclosure statement

containing at least the information required by Schedule H of Form ADV. Any additional information included in such disclosure shall be limited to information concerning wrap fee programs sponsored by the investment adviser.

- H. If the investment adviser is required under subsection (G) to furnish disclosure statements to clients or prospective clients of more than 1 wrap fee program, the investment adviser may omit from the disclosure statement furnished to clients and prospective clients of a wrap fee program or programs any information required by Schedule H that is not applicable to clients or prospective clients of that wrap fee program or programs.
- I. An investment adviser need not furnish the written disclosure statement required by subsection (G) to clients and prospective clients of a wrap fee program if another investment adviser is required to furnish and does furnish the written disclosure statement to all clients and prospective clients of the wrap fee program.

~~R14-6-206.—Custody of Client Funds or Securities by Investment Advisers~~

~~It shall constitute a fraudulent practice within the meaning of A.R.S. § 44-3241(A)(4) for any investment adviser to take or have custody of any securities or funds of any client unless:~~

- ~~1.—The investment adviser notifies the Commission in writing that the investment adviser has or may have custody of client funds or securities. Such notification may be given on Form ADV;~~
- ~~2.—The securities of each client are segregated, marked to identify the particular client having the beneficial interest therein, and held in safekeeping in some place reasonably free from risk of destruction or other loss;~~
- ~~3.—All client funds are deposited in 1 or more bank or similar accounts containing only clients' funds, such accounts are maintained in the name of the investment adviser as~~

~~agent or trustee for such clients, and the investment adviser maintains a separate record for each such account showing the name and address of the bank or similar institution where the account is maintained, the dates and amounts of deposits into and withdrawals from the account, and the exact amount of each client's beneficial interest in the account;~~

- ~~4. Immediately after accepting custody or possession of funds or securities from any client, the investment adviser notifies the client in writing of the place where and the manner in which the funds and securities will be maintained and, subsequently, if and when there is a change in the place where or the manner in which the funds or securities are maintained, the investment adviser gives prompt (but in no event more than 10 business days) written notice thereof to the client;~~
- ~~5. At least once every 3 months, the investment adviser sends each client an itemized statement showing the client's funds and securities in the investment adviser's custody at the end of such period and all debits, credits, and transactions in the client's account during such period; and~~
- ~~6. At least once every calendar year, an independent CPA or public accountant verifies all client funds and securities by actual examination at a time chosen by the independent CPA or public accountant without prior notice to the investment adviser. The independent CPA's or public accountant's report stating that such CPA or public accountant has made an examination of such funds and securities, and describing the nature and extent of the examination, shall be filed with the Commission promptly (but in no event more than 30 days) after each such examination.~~

R14-6-206. Custody of Client Funds or Securities by Investment Advisers

A. Except as otherwise provided in subsection (B), it shall constitute a fraudulent practice within the meaning of A.R.S. § 44-3241(A)(4) for any investment adviser to take or have custody of any securities or funds of any client unless:

1. The investment adviser notifies the Commission in writing that the investment adviser has or may have custody of client funds or securities. Such notification may be given on Form ADV.
2. The securities of each client are segregated, marked to identify the particular client having the beneficial interest therein, and held in safekeeping in some place reasonably free from risk of destruction or other loss.
3. All client funds are deposited in 1 or more bank or similar accounts containing only clients' funds, such accounts are maintained in the name of the investment adviser as agent or trustee for such clients, and the investment adviser maintains a separate record for each such account showing the name and address of the bank or similar institution where the account is maintained, the dates and amounts of deposits into and withdrawals from the account, and the exact amount of each client's beneficial interest in the account.
4. Immediately after accepting custody or possession of funds or securities from any client, the investment adviser notifies the client in writing of the place where and the manner in which the funds and securities will be maintained and, subsequently, if and when there is a change in the place where or the manner in which the funds or securities are maintained, the investment adviser gives written notice to the client within 10 business days.

5. At least once every 3 months, the investment adviser sends each client an itemized statement showing the client's funds and securities in the investment adviser's custody at the end of such period and all debits, credits, and transactions in the client's account during such period.
6. At least once every calendar year, an independent CPA or public accountant verifies all client funds and securities by actual examination at a time chosen by the independent CPA or public accountant without prior notice to the investment adviser. The independent CPA's or public accountant's report stating that such CPA or public accountant has made an examination of such funds and securities, and describing the nature and extent of the examination, shall be filed with the Commission within 30 calendar days after the examination.

B. With respect to federal covered advisers, the provisions of this Section only apply to the extent permitted by Section 203A of the Investment Advisers Act of 1940.

~~R14-6-207. Suitability of Investment Advisory Services~~

~~It shall constitute a fraudulent practice within the meaning of A.R.S. § 44-3241(A)(4) for any person providing investment advisory services to provide investment advisory services to any client, other than in connection with impersonal advisory services, unless the person:~~

- ~~1. Before providing any investment advisory services, and as appropriate thereafter, makes a reasonable inquiry of the client as to the financial situation, investment experience, and investment objectives of the client; and~~
- ~~2. Reasonably determines that the investment advisory services are suitable for the client based upon the information obtained from the client in accordance with subsection (1) above.~~

R14-6-207. Suitability of Investment Advisory Services

A. Except as otherwise provided in subsection (B), it shall constitute a fraudulent practice within the meaning of A.R.S. § 44-3241(A)(4) for any person to provide investment advisory services to any client, other than in connection with impersonal advisory services, unless the person:

1. Before providing any investment advisory services, and as appropriate thereafter, makes a reasonable inquiry of the client as to the financial situation, investment experience, and investment objectives of the client; and
2. Reasonably determines that the investment advisory services are suitable for the client based upon the information obtained from the client in accordance with subsection (A)(1) above.

B. With respect to federal covered advisers, the provisions of this Section only apply to the extent permitted by Section 203A of the Investment Advisers Act of 1940.

~~R14-6-208. Advertisements by Investment Advisers or Investment Adviser Representatives~~

~~A. It shall constitute a fraudulent practice within the meaning of A.R.S. § 44-3241(A)(4) for any investment adviser or investment adviser representative, directly or indirectly, to use any advertisement:~~

- ~~1. Which refers, directly or indirectly, to any testimonial of any kind concerning the investment adviser or investment adviser representative or concerning any advice, analysis, report, or other service rendered by such investment adviser; or~~
- ~~2. Which refers, directly or indirectly, to past specific recommendations of such investment adviser or investment adviser representative which were or would have been profitable to any person; provided, however, that this shall not prohibit an advertisement which~~

~~sets out or offers to furnish a list of all recommendations made by such investment adviser or investment adviser representative within the immediately preceding period of not less than 1 year if such advertisement, and such list if it is furnished separately:~~

- ~~a. States the name of each such security recommended, the date and nature of each such recommendation (for example, whether to buy, sell, or hold), the market price at that time, the price at which the recommendation was to be acted upon, and the market price of each such security as of the most recent practicable date; and~~
- ~~b. Contains the following cautionary legend on the 1st page thereof in print or type as large as the largest print or type used in the body or text thereof: "It should not be assumed that recommendations made in the future will be profitable or will equal the performance of the securities in this list;" or~~
- ~~3. Which represents, directly or indirectly, that any graph, chart, formula, or other device being offered can in and of itself be used to determine which securities to buy or sell, or when to buy or sell them; or which represents, directly or indirectly, that any graph, chart, formula, or other device being offered will assist any person in making his or her own decisions as to which securities to buy or sell, or when to buy or sell them, without prominently disclosing in such advertisement the limitations thereof and the difficulties with respect to its use; or~~
- ~~4. Which contains any statement to the effect that any report, analysis, or other service will be furnished free or without charge, unless such report, analysis or other service actually is or will be furnished entirely free and without any condition or obligation, directly or indirectly; or~~
- ~~5. Which states that the Commission has approved any advertisement.~~

~~B. When requested by the Commission, any advertisement used directly or indirectly in connection with the provision of investment advisory services shall be filed with the Commission at least 10 business days prior to its proposed use.~~

~~C. Any advertisement that has been requested by the Commission pursuant to the provisions of subsection (B) but that has not been filed with the Commission shall not be used.~~

R14-6-208. Advertisements by Investment Advisers or Investment Adviser Representatives

A. Except as otherwise provided in subsection (D), it shall constitute a fraudulent practice within the meaning of A.R.S. § 44-3241(A)(4) for any investment adviser or investment adviser representative, directly or indirectly, to use any advertisement:

1. Which refers, directly or indirectly, to any testimonial of any kind concerning the investment adviser or investment adviser representative or concerning any advice, analysis, report, or other service rendered by such investment adviser or investment adviser representative.
2. Which refers, directly or indirectly, to past specific recommendations of the investment adviser or investment adviser representative that were or would have been profitable to any person; except that an investment adviser or investment adviser representative may furnish or offer to furnish a list of all recommendations made by the investment adviser or investment adviser representative within the immediately preceding period of not less than 1 year if the investment adviser or investment adviser representative also furnishes:
 - a. The name of each security recommended, the date and nature of each recommendation (for example, whether to buy, sell, or hold), the market price at that time, the price at which the recommendation was to be acted upon, and the most recently available market price of each such security; and

- b. The following legend on the 1st page in prominent print or type: "It should not be assumed that recommendations made in the future will be profitable or will equal the performance of the securities in this list."
- 3. Which represents, directly or indirectly, that any graph, chart, formula, or other device being offered can in and of itself be used to determine which securities to buy or sell, or when to buy or sell them; or which represents, directly or indirectly, that any graph, chart, formula, or other device being offered will assist any person in making that person's own decisions as to which securities to buy or sell, or when to buy or sell them, without prominently disclosing in such advertisement the limitations thereof and the difficulties with respect to its use.
- 4. Which represents, directly or indirectly, that any report, analysis, or other service will be furnished for free or without charge, unless such report, analysis, or other service actually is or will be furnished entirely free and without any direct or indirect condition or obligation.
- 5. Which states that the Commission has approved any advertisement.
- B. When requested by the Commission, any advertisement used directly or indirectly in connection with the provision of investment advisory services shall be filed with the Commission at least 10 business days prior to its proposed use.
- C. Any advertisement that has been requested by the Commission pursuant to the provisions of subsection (B) but that has not been filed with the Commission shall not be used.
- D. With respect to federal covered advisers, the provisions of this Section only apply to the extent permitted by Section 203A of the Investment Advisers Act of 1940.

~~R14-6-209. Financial and Disciplinary Information that Investment Advisers Must Disclose to Clients~~

~~A. The following definitions shall apply to this Section:~~

- ~~1. "Investment related" means pertaining to securities, commodities, banking, insurance, or real estate (including, but not limited to, acting as or being associated with a broker-dealer, investment company, investment adviser, government securities broker or dealer, municipal securities dealer, bank, savings and loan association, entity, or person required to be registered under the Commodity Exchange Act, or fiduciary).~~
- ~~2. "Involved" means acting or aiding, abetting, causing, counseling, commanding, inducing, conspiring with, or failing reasonably to supervise another in doing an act.~~
- ~~3. "Management person" means a person with power to exercise, directly or indirectly, a controlling influence over the management or policies of an investment adviser which is a company or to determine the general investment advice given to clients.~~
- ~~4. "Self regulatory Organization" or "SRO" means any national securities or commodities exchange, registered association, or registered clearing agency.~~

~~B. It shall constitute a fraudulent practice within the meaning of A.R.S. § 44-3241(A)(4) for any investment adviser to fail to disclose to any client or prospective client all material facts with respect to:~~

- ~~1. A financial condition of the investment adviser that is reasonably likely to impair the ability of the investment adviser to meet contractual commitments to clients, if the investment adviser has discretionary authority (express or implied) or custody over such client's funds or securities, or requires prepayment of advisory fees of more than \$500 from such client, 6 months or more in advance; or~~

~~2.—A legal or disciplinary event that is material to an evaluation of the investment adviser's integrity or ability to meet contractual commitments to clients.~~

~~C.—It shall constitute a rebuttable presumption that the following legal or disciplinary events involving the investment adviser or a management person of the investment adviser (any of the foregoing being referred to hereafter as a "person") that were not resolved in the person's favor or subsequently reversed, suspended, or vacated are material within the meaning of subsection (B)(2) for a period of 10 years from the time of the event. No affirmative or negative presumption of materiality shall be created under subsection (B)(2) for events not specifically set forth in this subsection.~~

~~1.—A criminal or civil action in a court of competent jurisdiction in which the person:~~

~~a.—Was convicted, pleaded guilty or nolo contendere ("no contest") to a felony or misdemeanor, or is the named subject of a pending criminal proceeding (any of the foregoing referred to hereafter as "action"), and such action involved: an investment-related business; fraud, false statements, or omissions; wrongful taking of property; or bribery, forgery, counterfeiting, or extortion;~~

~~b.—Was found to have been involved in a violation of an investment-related statute or rule; or~~

~~c.—Was the subject of any order, judgment, or decree permanently or temporarily enjoining the person from, or otherwise limiting the person from, engaging in any investment-related activity.~~

~~2.—Administrative proceeding before the Securities and Exchange Commission, the Commission, or any federal regulatory agency or any state agency (any of the foregoing being referred to hereafter as "agency") in which the person:~~

a. ~~Was found to have caused an investment-related business to lose its authorization to do business; or~~

b. ~~Was found to have been involved in a violation of an investment-related statute or rule, and was the subject of an order by the agency denying, suspending, or revoking the authorization of the person to act in, or barring or suspending the person's association with, an investment-related business; or otherwise significantly limiting the person's investment-related activities.~~

3. ~~Self-regulatory Organization ("SRO") proceedings in which the person:~~

a. ~~Was found to have caused an investment-related business to lose its authorization to do business; or~~

b. ~~Was found to have been involved in a violation of the SRO's rules and was the subject of an order by the SRO barring or suspending the person from membership or from association with other members, or expelling the person from membership; fining the person more than \$2,500; or otherwise significantly limiting the person's investment-related activities.~~

D. ~~The information required to be disclosed by subsection (B) shall be disclosed to clients promptly but in no event later than 30 days after the occurrence of the event requiring disclosure, and to prospective clients not less than 48 hours prior to entering into any written or oral investment advisory contract, or no later than the time of entering into such contract if the client has the right to terminate the contract without penalty within 5 business days after entering into the contract.~~

E. ~~For purposes of calculating the 10-year period during which events are presumed to be material under subsection (C), the date of the reportable event shall be the date on which the~~

~~final order, judgment, or decree was entered, or the date on which any rights of appeal from preliminary orders, judgments, or decrees lapsed.~~

- F. ~~Compliance with subsection (C) shall not relieve any investment adviser from the disclosure obligations of subsection (B); compliance with subsection (B) shall not relieve any investment adviser from any other disclosure requirement under the Act, the rules thereunder, or under any other state or federal law. Note: Investment advisers may disclose this information to clients and prospective clients in their "brochure," the written disclosure statement to clients under R14-6-205, provided, that the delivery of the brochure satisfies the timing of disclosure requirements described in subsection (D).~~

R14-6-209. Financial and Disciplinary Information that Investment Advisers Shall Disclose to
Clients

- A. Except as otherwise provided in subsection (F), it shall constitute a fraudulent practice within the meaning of A.R.S. § 44-3241(A)(4) for any investment adviser to fail to disclose to any client or prospective client all material facts with respect to:
1. A financial condition of the investment adviser that is reasonably likely to impair the ability of the investment adviser to meet contractual commitments to clients, if the investment adviser has discretionary authority (express or implied) or custody over the client's funds or securities, or requires prepayment of advisory fees of more than \$500 from such client, 6 months or more in advance.
 2. A legal or disciplinary event that is material to an evaluation of the investment adviser's or an investment adviser representative's integrity or ability to meet contractual commitments to clients.

3. A failure to comply with any arbitration award issued in connection with doing business as an investment adviser or investment adviser representative or as a dealer or salesman as defined in A.R.S. Title 44, Chapter 12.

B. It shall constitute a rebuttable presumption that the following legal or disciplinary events involving the investment adviser, an investment adviser representative, or a management person of the investment adviser (any of the foregoing being referred to hereafter as a "person") that were not resolved in the person's favor or subsequently reversed, suspended, or vacated are material within the meaning of subsection (A)(2) for a period of 10 years from the time of the event. No affirmative or negative presumption of materiality shall be created under subsection (A)(2) for events not specifically set forth in this subsection.

1. A criminal or civil action in a court of competent jurisdiction in which the person:

- a. Was convicted or pleaded guilty or nolo contendere ("no contest") to a felony or misdemeanor, or is the named subject of a pending criminal proceeding (any of the foregoing referred to hereafter as "action"), and such action involved: an investment-related business; fraud, false statements, or omissions; wrongful taking of property; or bribery, forgery, counterfeiting, or extortion;
- b. Was found to have been involved in a violation of an investment-related statute or rule; or
- c. Was the subject of any order, judgment, or decree permanently or temporarily enjoining the person or otherwise limiting the person from engaging in any investment-related activity.

2. An administrative proceeding before the SEC, the Commission, or any federal or state agency (any of the foregoing being referred to hereafter as "agency") in which the person:
 - a. Was found to have caused an investment-related business to lose its authorization to do business; or
 - b. Was found to have been involved in a violation of an investment-related statute or rule, and was the subject of an order by the agency denying, suspending, or revoking the authorization of the person to act in, or barring or suspending the person's association with, an investment-related business; or otherwise significantly limiting the person's investment-related activities.
 3. SRO proceedings in which the person:
 - a. Was found to have caused an investment-related business to lose its authorization to do business; or
 - b. Was found to have been involved in a violation of the SRO's rules and was the subject of an order by the SRO barring or suspending the person from membership or from association with other members, or expelling the person from membership; fining the person more than \$2,500; or otherwise significantly limiting the person's investment-related activities.
- C. The information required to be disclosed by subsection (A) shall be disclosed to clients within 30 calendar days after the occurrence of the event requiring disclosure, and to prospective clients not less than 48 hours prior to entering into any written or oral investment advisory contract, or no later than the time of entering into such contract if the

client has the right to terminate the contract without penalty within 5 business days after entering into the contract.

- D. For purposes of calculating the 10-year period during which events are presumed to be material under subsection (B), the date of the reportable event shall be the date on which the final order, judgment, or decree was entered, or the date on which any rights of appeal from preliminary orders, judgments, or decrees lapsed.
- E. Compliance with subsection (B) shall not relieve any investment adviser from the disclosure obligations of subsection (A); compliance with subsection (A) shall not relieve any investment adviser from any other disclosure requirement under the IM Act, the rules thereunder, or under any other state or federal law. Investment advisers may disclose this information to clients and prospective clients in their "brochure," the written disclosure statement to clients under R14-6-205, provided, that the delivery of the brochure satisfies the timing of disclosure requirements described in subsection (C).
- F. With respect to federal covered advisers, the provisions of this Section only apply to the extent permitted by Section 203A of the Investment Advisers Act of 1940.

R14-6-210. Licensure of Investment Adviser Representatives

- A. The definition of investment adviser representative in A.R.S. § 44-1301 includes an individual employed by a federal covered adviser only if the individual has a place of business in Arizona and either:
 - 1. Is a supervised person and meets all of the following conditions:
 - a. Has more than 5 clients who are natural persons, other than excepted persons.
 - b. Has clients more than 10% of whom are natural persons, other than excepted persons.

- c. On a regular basis, solicits, meets with, or otherwise communicates with clients of the investment adviser or provides other than impersonal advisory services.
 - 2. Is not a supervised person.
- B. For purposes of this Section:
- 1. "Excepted person" means a natural person who:
 - a. Immediately after entering into the investment advisory contract with the investment adviser has at least \$750,000 under management with the investment adviser, or
 - b. The investment adviser reasonably believes, immediately prior to entering into the advisory contract, has a net worth, together with assets held jointly with a spouse, at the time the contract is entered into of more than \$1,500,000.
 - 2. "Supervised person" means any partner, officer, director, or other person occupying a similar status or performing similar functions, or employees of an investment adviser, or other person who provides investment advice on behalf of the investment adviser and is subject to the supervision and control of the investment adviser.
 - 3. "Place of business" means:
 - a. An office at which the investment adviser representative regularly provides investment advisory services, solicits, meets with, or otherwise communicates with clients, or
 - b. Any other location that is held out to the general public as a location at which the investment adviser representative provides investment advisory services, solicits, meets with, or otherwise communicates with clients.

- C. A person that employs 1 or more investment adviser representatives who solicit, offer, or negotiate for the sale of or sell investment advisory services on behalf of an investment adviser shall license as an investment adviser unless each investment adviser representative is also employed by the investment adviser on whose behalf the activity is conducted.

R14-6-211. Solicitation

- A. An individual shall not be included in the definition of investment adviser representative under A.R.S. § 44-3101(3)(d) if that individual meets both of the following conditions:
1. The individual does not on a regular basis give advice regarding, or recommend the services of, an investment adviser or an investment adviser representative.
 2. The individual does not accept or receive directly or indirectly any commission, fee, or other remuneration in connection with a referral to or recommendation of the services of an investment adviser or an investment adviser representative.
- B. The term "remuneration" shall be broadly construed, but shall not include the exchange of client referrals between professionals without an exchange of additional compensation.
- C. No individual or entity subject to an order or finding that denies, revokes, or suspends licensure or registration under the Securities Exchange Act of 1934, the Investment Advisers Act of 1940, the Securities Act, the IM Act, or the rules or regulations of an SRO may solicit, offer, or negotiate for the sale of or sell investment advisory services.

R14-6-212. Application, Notice Filing, and Renewal Requirements

- A. An application for licensure as an investment adviser under A.R.S. § 44-3153(B) shall include the following:
1. An original typewritten Form ADV with all information and exhibits required by the form.

2. An audited balance sheet if the investment adviser will have custody of client funds or if the investment adviser requires the payment of advisory fees six months or more in advance and in excess of \$500 for each client. The audited balance sheet shall be based on the investment adviser's fiscal year end, shall be prepared in accordance with generally accepted accounting principles, and shall be audited by an independent certified public accountant. The notes to the balance sheet shall state the principles used to prepare the balance sheet, the basis of included securities, and any other explanation required for clarity.
 3. A notarized affidavit of any officer, director, partner, member, trustee, or manager of the applicant stating:
 - a. That a review of the records of the investment adviser has been conducted.
 - b. Whether any investment adviser activity has been conducted with residents of Arizona prior to licensure as an investment adviser.
 4. If the applicant intends to have a branch office in Arizona, the address and name of a contact individual located at such branch.
 5. If part II of the Form ADV is not completed, the applicant shall submit a copy of the disclosure brochure the applicant gives or will give to clients.
 6. The documents and fees required for each investment adviser representative as described in subsection (C).
 7. The annual licensure fee required by A.R.S. § 44-3181(A).
- B. A notice filing under A.R.S. § 44-3153(D) shall include the following:
1. A manually signed and notarized Form ADV, part 1, page 1, or a copy of Form ADV, part 1, page 1, and an originally executed consent to service of process.

2. The documents and fees required for each investment adviser representative as described in subsection (C).
 3. The annual notice filing fee required by A.R.S. § 44-3181(A).
- C. An application for an investment adviser representative licensure under A.R.S. § 44-3156 shall include the following:
1. A complete Form U-4.
 2. Proof of successful completion of required examinations in accordance with A.A.C. R14-6-204.
 3. The annual licensure fee required by A.R.S. § 44-3181(A).
- D. For purposes of A.R.S. § 44-3158(A), a license of an investment adviser or an investment adviser representative shall be renewed upon receipt of the nonrefundable license fee prescribed in A.R.S. § 44-3181.
- E. For purposes of A.R.S. § 44-3153(E), a notice filing shall be renewed upon receipt of the nonrefundable license fee prescribed in A.R.S. § 44-3181.

Arizona Corporation Commission, Securities Division
Chapter 6, Corporation Commission—Investment Management
Article 1. General Provisions Relating to the Arizona Investment Management Act
Article 2. Duties of Investment Advisers and Investment Adviser Representatives

Economic, Small Business, and Consumer Impact Statement

A. Economic, small business, and consumer impact summary.

1. Proposed rulemaking.

The Arizona Corporation Commission (the "Commission") repeals and replaces Sections R14-6-101 through R14-6-104 and R14-6-201 through R14-6-209 and adds new Sections R14-6-106 and R14-6-210 through R14-6-212 (collectively the "IM Rules").

2. Summary of information included in this report.

The economic, small business, and consumer impact statement for the IM Rules analyzes the costs, savings, and benefits that accrue to the Commission, the office of the attorney general, the regulated public, and the general public. With the adoption of the proposed rules, the impact on established Commission procedures, Commission staff time, and other administrative costs is minimal. The estimated additional cost to the office of the attorney general is minimal. The benefits provided by the IM Rules are nonquantifiable. The IM Rules should benefit the Commission's relations with the regulated public because of increased uniformity with federal and other state laws, the addition of a provision for the distribution of information regarding products and services on the Internet, the clarification of the statutory definition of investment adviser representative, the inclusion of parameters to the term "solicit" as used in the Arizona Investment Management Act adopted in April 1994 (the "IM Act"), and the clarification of filing requirements for licensure and notice filings. The public will benefit from the continuation

of the licensing of, and imposition of standards on, persons providing financial services and the continued exclusion of nonqualified persons from the industry. The Commission anticipates that the proposed rulemaking may decrease and will not increase monitoring, record keeping, or reporting burdens on businesses or persons. The costs of implementation or enforcement are not increased or are only marginally increased and such increase does not equal or exceed the reduction in burdens.

3. Name and address of agency employees who may be contacted to submit or request additional data on the information included in this statement.

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B. Economic, small business, and consumer impact statement

The Arizona Corporation Commission (the "Commission") has not conducted any study and is not aware of any study that measure the cost of implementation or compliance with the rules promulgated under the Arizona Investment Management Act adopted in April 1994 (the "IM Act"). The time and dollar expenditures necessary to obtain such data are prohibitive. Adequate data, therefore, is not reasonably available to provide quantitative responses to the items required under A.R.S. § 41-155(B).

1. Proposed rulemaking.

The Commission repeals and replaces Sections R14-6-101 through R14-6-104 and R14-6-201 through R14-6-209 and adds new Sections R14-6-106 and R14-6-210 through R14-6-212 (collectively the "IM Rules") in order to: (i) correct technical errors within the Sections; (ii) reflect amendments to the United States Securities and Exchange Commission

rules regarding the regulation of investment advisers and investment adviser representatives; (iii) provide for the distribution of information regarding products and services on the Internet; (iv) clarify the statutory definition of investment adviser representative; (v) prescribe parameters to the term "solicit" as used in the IM Act; and (vi) clarify filing requirements for licensure and notice filings. A brief description of the Sections follows:

R14-6-101. Definitions: defines various terms used through the Sections.

R14-6-102. Scope of Provisions: states the legal authority for the Sections, provides for the waiver of strict adherence to a provision, and provides that the Arizona Corporation Commission's rules of Practice and Procedure apply when not in conflict with the proposed Sections.

R14-6-103. Severability: establishes the severability of the Sections and the provisions thereof in case any Section or subsection is deemed to be invalid.

R14-6-104. Enforcement of the Arizona Investment Management Act: provides that the Sections relating to enforcement matters are Sections A.A.C. R14-4-301 through R14-4-308.

R14-6-106. General Dissemination of Information on the Internet: establishes the circumstances under which investment advisers and investment adviser representatives may distribute information regarding products and services on the Internet prior to licensure in Arizona.

R14-6-201. Books and Records of Investment Advisers: requires investment advisers to comply with the provisions of the SEC's books and records rule; also requires the maintenance of certain additional records in separate files.

R14-6-202. Supervision: provides a safe harbor for investment advisers regarding their supervisory responsibilities by prescribing procedures for investment advisers to follow.

R14-6-203. Dishonest and Unethical Practices: provides guidance regarding which actions by investment advisers and investment adviser representatives will be construed to fall within the term "dishonest or unethical" for purposes of A.R.S. § 44-3201(A)(13).

R14-6-205. Information to be Furnished to Clients ("Brochure Rule"): prescribes information that must be furnished to clients and the timing and method of such disclosure.

R14-6-206. Custody of Client Funds or Securities by Investment Advisers: provides that it is a fraudulent practice under the IM Act for an investment adviser to fail to comply with the procedures prescribed in the Section when maintaining custody of a client's funds or securities.

R14-6-207. Suitability of Investment Advisory Services: provides that it is a fraudulent practice under the IM Act for an investment adviser to fail to provide suitable investment advice based on a reasonable inquiry of the client's financial situation, investment experience, and investment objectives.

R14-6-208. Advertisements by Investment Advisers or Investment Adviser Representatives: provides that it is a fraudulent practice under the IM Act for an investment adviser or investment adviser representative to fail to comply with the limitations on advertising and the requirements prescribed in the Section.

R14-6-209. Financial and Disciplinary Information that Investment Advisers Shall Disclose to Clients: provides that it is a fraudulent practice for an investment adviser to fail to disclose to any client or prospective client all material facts with respect to (1) a financial

condition that is reasonably likely to impair the adviser's ability to meet contractual commitments to clients where the adviser has discretionary authority, custody, or requires prepayments of fees, (2) a legal or disciplinary event that is material to the evaluation of the adviser's integrity or ability to meet contractual commitments to clients, or (3) a failure to comply with an arbitration award.

R14-6-210. Licensure of Investment Adviser Representatives: provides the circumstances under which investment adviser representatives who are employed by federally registered investment advisers must be licensed in Arizona. Also provides that a person employing investment adviser representatives who solicit on behalf of another investment adviser must license as an investment adviser.

R14-6-211. Solicitation: defines the activities that do not constitute solicitation for purposes of A.R.S. § 44-3101(3)(d).

R14-6-212. Application, Notice Filing, and Renewal Requirements: enumerates the specific filing requirements for licensure, notice filings, and renewal of licensure and notice filings.

2. Persons who will be directly affected by, bear the costs of, or directly benefit from the proposed rulemaking.

Those affected by the IM rules include persons that are within the scope of the definition of investment advisers or investment adviser representatives contained in A.R.S. § 44-3101 (the "regulated persons") and persons who utilize their services. During the fiscal year 1999, the Commission licensed approximately 230 investment advisers and 444 investment adviser representatives. The Commission received approximately 550 notice filings from federally registered investment advisers.

Cost bearers.

The costs of compliance with the IM Rules will be borne directly by the regulated persons. The costs of enforcement of the IM Rules will be borne by the Commission and the office of the attorney general. The costs of implementation of the proposed rulemaking will be borne by the Commission.

The costs of compliance and enforcement remain substantially the same as under the IM Rules adopted July 19, 1996. The costs of implementation are minimal. The Commission anticipates that the proposed rulemaking may decrease, and will not increase, monitoring, record keeping, or reporting burdens on businesses or persons. The costs of implementation or enforcement are not increased or are only marginally increased and such increase does not equal or exceed the reduction in burdens.

Beneficiaries.

Persons seeking the services of investment advisers and investment adviser representatives will benefit from the continued licensure of, and imposition of standards on, investment advisers and investment adviser representatives. The public will benefit from continued exclusion of unqualified persons from the industry.

3. Cost/benefit analysis.

a. Cost/benefit analysis of the probable costs and benefits to the implementing agency and other agencies directly affected by the implementation and enforcement of the proposed rulemaking.

The benefits of the proposed rulemaking outweigh the probable costs. The implementation costs to the Commission are minimal because the systems, forms, etc., implemented in connection with the IM Rules adopted July 19, 1996, will not vary

materially. The costs to the Commission and the office of the attorney general to enforce the proposed rules remain substantially the same as the costs incurred under the IM Rules adopted July 19, 1996. The Commission and the office of the attorney general will benefit from the changes in the IM Rules, which will (i) correct technical errors within the Sections; (ii) reflect amendments to the United States Securities and Exchange Commission rules regarding the regulation of investment advisers and investment adviser representatives; (iii) provide for the distribution of information regarding products and services on the Internet; (iv) clarify the statutory definition of investment adviser representative; (v) prescribe parameters to the term "solicit" as used in the IM Act; and (vi) clarify filing requirements for licensure and notice filings.

b. Cost/benefit analysis of the probable costs and benefits to a political subdivision of this state directly affected by the implementation and enforcement of the proposed rulemaking.

None.

c. Cost/benefit analysis of the probable costs and benefits to businesses directly affected by the proposed rulemaking, including any anticipated effect on the revenues or payroll expenditures of employers who are subject to the proposed rulemaking.

The benefits of the proposed rulemaking outweigh the probable costs. The Commission anticipates that the costs of compliance by regulated persons will be substantially the same as those incurred in connection with compliance with the IM Rules adopted July 19, 1996. The Commission does not anticipate any effect on the revenues or payroll expenditures of regulated persons.

Regulated persons should benefit from the changes to the IM Rules, which will (i) correct technical errors within the Sections; (ii) reflect amendments to the United States Securities and Exchange Commission rules regarding the regulation of investment advisers and investment adviser representatives; (iii) provide for the distribution of information regarding products and services on the Internet; (iv) clarify the statutory definition of investment adviser representative; (v) prescribe parameters to the term "solicit" as used in the IM Act; and (vi) clarify filing requirements for licensure and notice filings.

4. General description of the probable impact on private and public employment in businesses, agencies, and political subdivisions of this state directly affected by the proposed rulemaking.

The Commission anticipates that the impact of the proposed rulemaking on public and private employment will be minimal because the proposed rulemaking incorporates in large part benefits and requirements contained in the IM Rules adopted July 19, 1996.

5. Statement of the probable impact of the proposed rulemaking on small businesses.

a. An identification of the small businesses subject to the proposed rulemaking.

Regulated persons are subject to the proposed rulemaking. The Commission anticipates that regulated persons licensed under the IM Act typically may be small businesses because investment advisers with assets under management of not less than \$25,000,000 register with the Securities and Exchange Commission under the Investment Advisers Act of 1940. States are precluded from requiring state licensure of federally registered investment advisers.

b. The administrative and other costs required for compliance with the proposed rulemaking.

The cost of compliance with the IM Rules may be decreased from the cost of compliance with the IM Rules adopted July 19, 1996, because the proposed rulemaking: reflects amendments to the United States Securities and Exchange Commission rules regarding the regulation of investment advisers and investment adviser representatives, increasing uniformity with federal laws and the laws of other states; provides for the distribution of information regarding products and services on the Internet without requiring licensure for solely that activity; clarifies the statutory definition of investment adviser representative; prescribes parameters to the IM Act; and clarifies filing requirements for licensure and notice filings.

c. A description of the methods that the agency may use to reduce the impact on small businesses.

The IM Rules impose only on regulated persons, which may include small businesses, that regulation deemed necessary and appropriate under the IM Act. The proposed rulemaking package includes changes that may reduce the impact of compliance, described above.

d. The probable cost and benefit to private persons and consumers who are directly affected by the proposed rulemaking.

Nonregulated persons and consumers will bear no direct cost as a result of the proposed rulemaking package. Persons seeking the services of investment advisers and investment adviser representatives will benefit from the continued licensure of, and imposition of standards on, investment advisers and investment adviser representatives.

6. Statement of the probable effect on state revenues.

The Commission anticipates that the effect on state revenues of the proposed rulemaking will be minimal because the proposed rulemaking incorporates the same fee structure contained in the IM Rules adopted July 19, 1996.

7. Description of any less intrusive or less costly alternative methods of achieving the purpose of the proposed rulemaking.

The goal of the proposed rulemaking is to effectuate the least intrusive and costly method of regulation of investment advisers and investment adviser representative required to achieve the statutorily mandated level of public protection.

AGENCY CERTIFICATE
Notice of Final Rulemaking

1. **Agency name:** Arizona Corporation Commission, Securities Division
2. **Chapter heading:** Chapter 6. Corporation Commission—Investment Management
3. **Code citation for Chapter:** 14 A.A.C. 6
4. **The Subchapters, if applicable; the Articles; the Parts, if applicable; and the**

Sections involved in the rulemaking, listed in numerical order:

Subchapters, Articles, Parts, and Sections

Action

Article 1. General Provisions Relating to the Arizona Investment Management Act

A.A.C. R14-6-101	Repeal
A.A.C. R14-6-101	New section
A.A.C. R14-6-102	Repeal
A.A.C. R14-6-102	New section
A.A.C. R14-6-103	Repeal
A.A.C. R14-6-103	New section
A.A.C. R14-6-104	Repeal
A.A.C. R14-6-104	New section
A.A.C. R14-6-106	New section

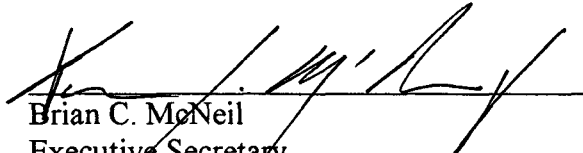
Article 2. Duties of Investment Advisers and Investment Adviser Representatives

A.A.C. R14-6-201	Repeal
A.A.C. R14-6-201	New section
A.A.C. R14-6-202	Repeal
A.A.C. R14-6-202	New section
A.A.C. R14-6-203	Repeal
A.A.C. R14-6-203	New section
A.A.C. R14-6-205	Repeal
A.A.C. R14-6-205	New section
A.A.C. R14-6-206	Repeal
A.A.C. R14-6-206	New section
A.A.C. R14-6-207	Repeal
A.A.C. R14-6-207	New section
A.A.C. R14-6-208	Repeal
A.A.C. R14-6-208	New section
A.A.C. R14-6-209	Repeal

A.A.C. R14-6-209
A.A.C. R14-6-210
A.A.C. R14-6-211
A.A.C. R14-6-212

New section
New section
New section
New section

5. The rules being submitted are true and correct versions of the rules made by the agency.


Brian C. McNeil
Executive Secretary
Arizona Corporation Commission

10 JAN 00
Date

6. Exempt from Governor's Regulatory Review Council: A.R.S. § 41-1057